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September 15, 2008

## **AGENDA ITEM 4b**

### **TO: MEMBERS OF THE INVESTMENT COMMITTEE**

- I. SUBJECT:** Update on Implementation of Asset Allocation Strategy
- II. PROGRAM:** Total Fund
- III. RECOMMENDATION:** Information
- IV. ANALYSIS:**

#### **BACKGROUND**

The purpose of this Item is to update the Investment Committee on the implementation of the new Asset Allocation Policy adopted in December 2007. The new policy and old policy target weights are shown in Attachment 1.

The major changes in the new policy are, by asset class:

- a) Decrease in Global Equity from 60% to 56%
- b) Increase in AIM from 6% to 10%
- c) Decrease in Fixed Income from 26% to 19%
- d) Increase in ILAC from 0% to 5%
- e) Increase in Real Estate from 8% to 10%

In order to implement this change over a multi-year period Staff worked with Wilshire Associates to develop quarterly interim policy (target) asset class allocations for 2008. Interim target and actual weightings are listed in Attachment 1.

## 2008 INTERIM TARGETS BY ASSET CLASS

### **Global Equity (GE)**

Historically GE has been overweighted in the CalPERS portfolio. In the second half of 2007 the GE overweight was reduced to an underweight position of 58.2% relative to the 60% target as of September 30, 2007. In Q4 the GE underweight was further increased due to Staff tactical underweight as well as equity market decline. As a result, by December 31, 2007 the GE weight was reduced to 56.2% and this made the transition to the new target of 56% easier when it was adopted in December 2007. Hence the interim policy target for GE was set at 56% starting in Q1 2008. The Staff tactical underweight to GE continues with a 3% underweight at the end of June 2008.

### **Alternative Investments (AIM)**

The AIM exposure was 8.1% as of December 31, 2007 compared to the old target of 6.0%. The 2008 interim policy targets for AIM were set at 9.0% in Q1 and Q2 and increased to 9.5% in Q3 and Q4. At the end of June 2008, the actual AIM allocation was 10.3% or 1.3% above benchmark weight. The overweight in private equities (AIM) partly offsets the underweight in publicly traded equities (Global Equity).

### **Global Fixed Income (GFI)**

GFI was overweighted by 0.7% relative to the old target of 26% as of December 31, 2007. The 2008 interim targets for GFI were set at 25% in Q1, 23.5% in Q2 and 22.5% in Q3 and Q4. GFI will be the source of funding for all other asset classes in this period. GFI was overweight by 1.9% at the end of March and by 1.2% at the end of June 2008 because of Staff's decision to overweight fixed income relative to equities.

### **Inflation-Linked Assets (ILAC)**

The ILAC assets transferred from Real Estate and AIM were about 0.8% as of December 31, 2007. The ILAC 2008 interim targets were set at 1.0% in Q1, 1.5% in Q2, and 2.0% in Q3 and Q4. ILAC actual allocations have slightly exceeded benchmark weights.

### **Real Estate (RE)**

RE weight was 8.2% as of December 31, 2007. The 2008 interim policy targets for RE are 9% in Q1, and 10.0% in Q2, Q3, and Q4. RE actual allocations have approximated benchmark weights.

These quarterly interim policy targets for 2008 will be used by Wilshire to calculate the policy return for the Total Fund in this period. Interim policy targets for 2009 will be determined by Staff and agreed upon with Wilshire prior to December 31, 2008.

Staff expects the implementation of the new policy targets to be completed by the end of 2010.

### **V. STRATEGIC PLAN:**

This item is consistent with Strategic Plan Goal VIII, manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first, to pay benefits, and second, to minimize and stabilize contributions. This item is also consistent with Goal IX; achieve long-term, sustainable, risk-adjusted returns.

### **VI. RESULTS/COSTS:**

This item is not expected to have any material cost.

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